BBA Corporate Finance, class 1.

1. What are major types of firms ?
2. Describe major characteristics of each type, including the means for distributing income to owners.
3. Distinguish between limited and unlimited liability, and list firm types that are subject to each type of liability.
4. List the four major financial statements required by the SEC for publicly traded firms, define each of the four statements, and explain why each of these financial statements is valuable.
5. Discuss the difference between book value of stockholders’ equity and market value of stockholders’ equity; explain why the two numbers are almost never the same?
6. What is ratio analysis?
7. Define the term “competitive market,” give examples of markets that are competitive and some that aren’t, and discuss the importance of a competitive market in determining the value of a good.
8. Explain why maximizing NPV is always the correct decision rule.
9. Define arbitrage, and discuss its role in asset pricing. How does it relate to the Law of One Price?
10. Differentiate between two types of cash flows (inflows, outflows).
11. Explain the Three Rules of Time Travel.
12. Explain perpetuities.
13. Explain annuities.
14. Explain internal rate of return (IRR).

1) A sole proprietorship is owned by:

A) one person.

B) two of more persons.

C) shareholders.

D) bankers.

2) Which of the following organization forms for a business does NOT avoid double taxation?

A) Limited partnership

B) "C" corporation

C) "S" corporation

D) Limited liability company

5) Which of the following is NOT an advantage of a sole proprietorship?

A) Single taxation

B) Ease of setup

C) Limited liability

D) No separation of ownership and control

6) Which of the following statements regarding limited partnerships is TRUE?

A) There is no limit on a limited partner's liability.

B) A limited partner's liability is limited by the amount of their investment.

C) A limited partner is not liable until all the assets of the general partners have been exhausted.

D) A general partner's liability is limited by the amount of their investment.

7) Which of the following is/are an advantage of incorporation?

A) Access to capital markets

B) Limited liability

C) Unlimited life

D) All of the above

1.2 Ownership Versus Control of Corporations

1) In a corporation, the ultimate decisions regarding business matters are made by:

A) the Board of Directors.

B) debt holders.

C) shareholders.

D) investors.

2) The person charged with running the corporation by instituting the rules and policies set by the board of directors is called:

A) the chief operating officer.

B) the company president.

C) the chief executive officer.

D) the chief financial officer.

3) The Principal-Agent Problem arises:

A) because managers have little incentive to work in the interest of shareholders when this means working against their own self-interest.

B) because of the separation of ownership and control in a corporation.

C) Both A and B

D) None of the above

7) The most senior financial manager in a corporation is usually called:

A) the chief executive officer.

B) the chief financial officer.

C) the chief operating officer.

D) the chairman of the board.

1.3 The Stock Market

*Use the table for the question(s) below.*

Consider the following two quotes for XYZ stock:

1) How much would you have to pay to purchase 100 shares of XYZ stock on November 18th?

|  |  |  |  |
| --- | --- | --- | --- |
| **November 11th** | | **November 18th** | |
| Ask: | 25.25 | Ask: | 26.00 |
| Bid: | 25.20 | Bid: | 25.93 |

A) $2520

B) $2525

C) $2593

D) $2600

2) How much would you receive if you sold 200 shares of XYZ stock on November 11th?

|  |  |  |  |
| --- | --- | --- | --- |
| **November 11th** | | **November 18th** | |
| Ask: | 25.25 | Ask: | 26.00 |
| Bid: | 25.20 | Bid: | 25.93 |

A) $5050

B) $5040

C) $5186

D) $5200

5) An investment is said to be liquid if the investment:

A) has large day to day fluctuations in price.

B) has a large bid-ask spread.

C) can easily be converted into cash.

D) is traded on a stock exchange.

6) What type of company trades on an organized stock exchange?

A) A limited liability company

B) A private company

C) An "S" corporation

D) A public company

8) If you buy shares of Coca-Cola on the primary market:

A) Coca-Cola receives the money because the company has issued new shares.

B) you buy the shares from another investor who decided to sell the shares.

C) you buy the shares from the New York Stock Exchange.

D) you buy the shares from the Federal Reserve.

9) If you buy shares of Coca-Cola on the secondary market:

A) Coca-Cola receives the money because the company has issued new shares.

B) you buy the shares from another investor who decided to sell the shares.

C) you buy the shares from the New York Stock Exchange.

D) you buy the shares from the Federal Reserve.

Consider the following two quotes for XYZ stock:

|  |  |  |  |
| --- | --- | --- | --- |
| **November 11th** | | **November 18th** | |
| Ask: | 25.25 | Ask: | 26.00 |
| Bid: | 25.20 | Bid: | 25.93 |

10) What are your net proceeds if you purchased 2500 shares of XYZ stock on November 11th and then sold them a week later on November 18th?

***Corporate Finance, 4e, Global Edition* (Berk / DeMarzo)**

**Chapter 2 Introduction to Financial Statement Analysis**

2.1 Firms' Disclosure of Financial Information

2) Which of the following is NOT a financial statement that every public company is required to produce?

A) Income Statement

B) Statement of Sources and Uses of Cash

C) Balance Sheet

D) Statement of Stockholders' Equity

3) The third party who checks annual financial statements to ensure that they are prepared according to GAAP and verifies that the information reported is reliable is the:

A) NYSE Enforcement Board.

B) Accounting Standards Board.

C) Securities and Exchange Commission (SEC).

D) auditor.

2.2 The Balance Sheet

1) Which of the following balance sheet equations is INCORRECT?

A) Assets - Liabilities = Shareholders' Equity

B) Assets = Liabilities + Shareholders' Equity

C) Assets - Current Liabilities = Long Term Liabilities

D) Assets - Current Liabilities = Long Term Liabilities + Shareholders' Equity

2.3 The Income Statement

1) Which of the following statements regarding the income statement is INCORRECT?

A) The income statement shows the earnings and expenses at a given point in time.

B) The income statement shows the flow of earnings and expenses generated by the firm between two dates.

C) The last or "bottom" line of the income statement shows the firm's net income.

D) The first line of an income statement lists the revenues from the sales of products or services.

In November 2009, Perrigo Co. (PRGO) had a share price of $39.20. They had 91.33 million shares outstanding, a market-to-book ratio of 3.76. In addition, PRGO had $845.01 million in outstanding debt, $163.82 million in net income, and cash of $257.09 million.

15) Perrigo's market capitalization is closest to:

A) $952.16 million

B) $3580.14 million

C) $4168.06 million

D) $4425.15 million

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6) Perrigo's earnings per share (EPS) is closest to:

A) $0.19

B) $1.79

C) $2.81

D) $3.76

2.4 The Statement of Cash Flows

1) Which of the following is NOT a section on the cash flow statement?

A) Income generating activities

B) Investing activities

C) Operating activities

D) Financing activities

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**Chapter 3 Financial Decision Making and the Law of One Price**

3.1 Valuing Decisions

1) Due to a pre-existing contract, Recycle America Inc. has the opportunity to acquire 10,000 pounds of scrap aluminum and 2500 pounds of scrap lead for $10,750. If the current market price for scrap aluminum is $0.83 per pound and the current market price for lead is $1.06 per pound, then the added benefit (cost) to you if you acquire this metal is:

A) ($200)

B) $200

C) ($1925)

D) $1925

3.2 Interest Rates and the Time Value of Money

1) If the risk-free rate of interest (*rf*) is 3.5%, then you should be indifferent between receiving $1000 in one-year or:

A) $965.00 today.

B) $966.18 today.

C) $1000.00 today.

D) $1035.00 today.

2) Suppose you have $1000 today and the risk-free rate of interest (*rf*) is 3.5%. The equivalent value in one year is closest to:

A) $965.00 today.

B) $966.18 today.

C) $1000.00 today.

D) $1035.00 today.

10) When we express the value of a cash flow or series of cash flows in terms of dollars today, we call it the \_\_\_\_\_\_\_\_ of the investment. If we express it in terms of dollars in the future, we call it the \_\_\_\_\_\_\_\_.

A) present value; future value

B) future value; present value

C) ordinary annuity; annuity due

D) discount factor; discount rate

14) You are offered an investment opportunity in which you will receive $25,000 in one year in exchange for paying $23,750 today. Suppose the risk-free interest rate is 6% per year. Should you take this project? The NPV for this project is closest to:

A) Yes; NPV = $165

B) No; NPV = $165

C) Yes; NPV = -$165

D) No; NPV = -$165

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**Chapter 4 The Time Value of Money**

4.2 The Three Rules of Time Travel

1) Which of the following statements is FALSE?

A) The process of moving a value or cash flow forward in time is known as compounding.

B) The effect of earning interest on interest is known as compound interest.

C) It is only possible to compare or combine values at the same point in time.

D) A dollar in the future is worth more than a dollar today.

2) Which of the following statements is FALSE?

A) Finding the present value and compounding are the same.

B) A dollar today and a dollar in one year are not equivalent.

C) If you want to compare or combine cash flows that occur at different points in time, you first need to convert the cash flows into the same units or move them to the same point in time.

D) The equivalent value of two cash flows at two different points in time is sometimes referred to as the time value of money.

3) At an annual interest rate of 7%, the future value of $5000 in five years is closest to:

A) $3565

B) $6750

C) $7015

D) $7035

4) At an annual interest rate of 7%, the present value of $5000 received in five years is closest to:

A) $3565

B) $6750

C) $7015

D) $7035

7) Your great aunt Matilda put some money in an account for you on the day you were born. This account pays 8% interest per year. On your 21st birthday the account balance was $5033.83.

The amount of money that your great aunt Matilda originally put in the account is closest to:

A) $600

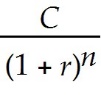
B) $800

C) $1000

D) $1200

9) Which of the following statements is FALSE?

A) The process of moving a value or cash flow backward in time is known as discounting.

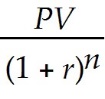
B) *FV* = 

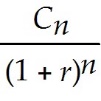
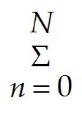
C) The process of moving a value or cash flow forward in time is known as compounding.

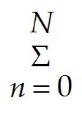
D) The value of a cash flow that is moved forward in time is known as its future value.

4.3 Valuing a Stream of Cash Flows

2) Which of the following statements is FALSE?

A) *FV* = 

B) *PV* = 

C) *FV* = *Cn* × (1 + *r*)*n*

D) Most investment opportunities have multiple cash flows that occur at different points in time.

4.4 Calculating the Net Present Value

1) Nielson Motors is considering an opportunity that requires an investment of $1,000,000 today and will provide $250,000 one year from now, $450,000 two years from now, and $650,000 three years from now. If the appropriate interest rate is 10%, then the NPV of this opportunity is closest to:

A) ($88,000)

B) $88,000

C) $300,000

D) $1,300,000

4) Kampgrounds Inc. is considering purchasing a parcel of wilderness land near a popular historic site. Although this land will cost Kampgrounds $400,000 today, by renting out wilderness campsites on this land, Kampgrounds expects to make $35,000 at the end of every year indefinitely. If the appropriate discount rate is 8%, then the NPV of this new wilderness campsite is closest to:

A) -$50,000

B) -$37,500

C) $37,500

D) $50,000

4.5 Perpetuities and Annuities

1) Which of the following statements regarding perpetuities is FALSE?

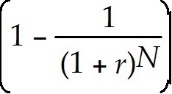
A) To find the value of a perpetuity one cash flow at a time would take forever.

B) A perpetuity is a stream of equal cash flows that occurs at regular intervals and lasts forever.

C) *PV* of a perpetuity = **

D) One example of a perpetuity is the British government bond called a consol.

2) Which of the following statements regarding annuities is FALSE?

A) *PV* of an annuity = *C* × 

B) The difference between an annuity and a perpetuity is that a perpetuity ends after some fixed number of payments.

C) An annuity is a stream of N equal cash flows paid at regular intervals.

D) Most car loans, mortgages, and some bonds are annuities.

9) The British government has a consol bond outstanding that pays ₤100 in interest each year. Assuming that the current interest rate in Great Britain is 5% and that you will receive your first interest payment one year from now, then the value of the consol bond is closest to:

A) ₤1000

B) ₤1100

C) ₤2100

D) ₤2000